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Arizona Corporation Commission

BEFORE THE ARIZONA CORPORATION COMMISSION

DOCKETED

JUN 22 1998

JIM IRVIN
COMMISSIONER - CHAIRMAN
RENZ D. JENNINGS
COMMISSIONER
CARL J. KUNASEK
COMMISSIONER

DOCKETED BY

C.M.

IN THE MATTER OF THE COMPETITION IN
THE PROVISION OF ELECTRIC SERVICES
THROUGHOUT THE STATE OF ARIZONA.

DOCKET NO. RE-00000C-94-0165

DECISION NO. 60977

OPINION AND ORDER

DATES OF HEARING:

December 9, 1997 and February 5, 1998 (Procedural
Conferences); February 9, 10, 11, 12, 13, 17, 18, 19, 20,
23, 25, 26 and 27, 1998

PLACE OF HEARING:

Phoenix, Arizona

PRESIDING OFFICER:

Jerry L. Rudibaugh

IN ATTENDANCE:

Renz D. Jennings, Commissioner
Carl J. Kunasek, Commissioner

APPEARANCES:

Mr. Steven M. Wheeler, Mr. Thomas L. Mumaw and Mr.
Jeffrey B. Guldner, SNELL & WILMER, LLP, on behalf
of Arizona Public Service Company;

Ms. Deborah R. Scott and Ms. Teena Wolfe, on behalf of
the Residential Utility Consumer Office;

Mr. Raymond S. Heyman, ROSHKA, HEYMAN &
DEWULF, P.C., and Mr. Bradley S. Carroll, on behalf of
Tucson Electric Power Company;

Mr. Craig A. Marks, on behalf of Citizens Utilities
Company;

Mr. Lex J. Smith, BROWN and BAIN, P.A., on behalf of
Ajo Improvement Company, Morenci Water and Electric
Company, and Phelps Dodge Corporation;

Mr. Michael M. Grant, GALLAGHER & KENNEDY, on
behalf of Arizona Electric Power Cooperative, Graham
County Electric Cooperative, and Duncan Valley Electric
Cooperative;

Mr. Walter W. Meek, President, on behalf of Arizona
Utility Investors Association;

Mr. Norman J. Furuta, on behalf of the Department of the
Navy;

1 Ms. Betty Pruitt on behalf of Arizona Community Action
2 Association;

3 Mr. C. Webb Crockett and Mr. Jay L. Shapiro,
4 FENNEMORE CRAIG, on behalf of Cyprus Climax
Metals, Co., ASARCO, Inc., and Arizonans for Electric
Choice and Competition;

5 Mr. Robert S. Lynch on behalf of Arizona Transmission
6 Dependent Utility Group;

7 Mr. Douglas C. Nelson and Mr. Michael B. Day,
8 GOODIN, MACBRIDE, SQUERI, SCHLOTZ &
9 RITCHIE, LLP, on behalf of Electric Competition
Coalition, Enron Corporation and Enron Energy Services,
Inc.;

10 Mr. Lawrence V. Robertson, Jr., MUNGER CHADWICK,
on behalf of PG&E Energy Services and Arizona School
Boards Association;

11 Ms. Barbara Sherman and Ms. Marcia Weeks on behalf of
12 Arizona Consumers Council;

13 Ms. Suzanne M. Dallimore, Antitrust Unit Chief, on behalf
14 of the Arizona Attorney General's Office;

15 Ms. Loretta Humphrey, Civil Division, on behalf of the
City of Tucson;

16 Mr. William P. Sullivan, MARTINEZ & CURTIS, P.C.,
17 on behalf of Navopache Electric Cooperative;

18 Ms. Elizabeth S. Firkins on behalf of International
Brotherhood of Electrical Workers, L.U. #1116;

19 Mr. Carl Dabelstein in pro persona;

20 Mr. Myron L. Scott on behalf of Arizonans for a Better
21 Environment;

22 Mr. Andrew W. Bettwy on behalf of Southwest Gas
Corporation; and

23 Mr. Paul A. Bullis, Chief Counsel, Mr. Christopher C.
24 Kempley, Assistant Chief Counsel and Ms. Janice M.
Alward, Staff Attorney, on behalf of the Utilities Division
25 of the Arizona Corporation Commission.
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BY THE COMMISSION:

The Arizona Corporation Commission ("Commission") issued Decision No. 59943, dated December 26, 1996, which approved new rules, A.A.C. R14-2-1601 through R14-2-1616 ("Rules" or "Electric Competition Rules"). On August 29, 1997, the Commission issued Decision No. 60351, in which the Hearing Division was directed "to produce procedural orders in order to establish hearings, evidentiary or otherwise, regarding any aspect of electric competition that is necessary and appropriate."

On October 30, 1997, the Residential Utility Consumer Office ("RUCO") filed a Request for Evidentiary Hearing and Procedural Order ("Request for Hearing"). On November 21, 1997, Tucson Electric Power Company ("TEP") filed a Response in support of RUCO's Request for Hearing. On November 21, 1997, Citizens Utilities Company ("Citizens") filed a Statement in support of RUCO's Request for Hearing.

On November 13, 1997, ASARCO Incorporated, Cyprus Climax Metal Corporation and Enron Corporation filed their Objection to RUCO's Request. On November 15, 1997, the Electric Competition Coalition filed its Objection to RUCO's Request.

The Electric Competition Rules created several working groups that were required to generate reports regarding various aspects of the transition to competition. On September 30, 1997, the Stranded Cost Working Group ("Group") filed its Report with the Commission. The Group provided an oral presentation to the Commission on November 25, 1997.

Pursuant to Decision No. 60351 and A.A.C. R14-3-109, our December 1, 1997 Procedural Order set an evidentiary hearing on generic issues related to stranded costs and scheduled a December 9, 1997 Procedural Conference. The following were participants in the December 9, 1997 Procedural Conference and were designated as parties in this matter:

Arizona Electric Power Cooperative ("AEPCO")
 Arizona Community Action Association ("ACAA")
 Ft. Huachuca ("FTH")
 State of Arizona, Attorney General's Office ("Attorney General")
 Safford, Wickenburg Irrigation & Electric District
 Salt River Project Agricultural Improvement and Power District ("SRP")¹
 Irrigation and Electrical District of Arizona
 PG&E Energy Services ("PG&E")

¹ Subsequently, SRP withdrew from the proceeding.

1 Arizona Utility Investors Association ("AUIA")
 2 Morenci Water & Electric, Ajo Improvement Co ("Morenci" and "Ajo")
 3 Residential Utility Consumer Office
 4 Citizens Utilities Company
 5 City of Tucson
 6 Arizona Public Service Company ("APS")
 7 Tucson Electric Power Company
 8 Cyprus Climax Metals Co. ("Cyprus")
 9 Electric Competition Coalition
 10 Arizonans for Electric Choice and Competition
 11 Enron Corporation ("Enron")
 12 ASARCO Incorporated
 13 Staff of the Arizona Corporation Commission ("Staff")

14 The following additional entities requested and were granted intervention:

15 Goldwater Institute
 16 Land and Water Fund
 17 Mohave Electric Cooperative, Inc.
 18 Navopache Electric Cooperative, Inc.
 19 Arizona Consumers Council
 20 BHP Copper, Inc.
 21 Mr. Carl Dabelstein
 22 Arizona Municipal Power Users' Association
 23 City of Phoenix
 24 Arizonans for a Better Environment
 25 Arizona Transmission Dependent Utility Group ("Utility Group")
 26 Southwest Gas Corporation
 27 Trico Electric Cooperative, Inc.
 28 Sulphur Springs
 Graham County Electric Cooperative, Inc.
 Duncan Valley Electric Cooperative, Inc.
 City of Scottsdale
 Arizona School Boards Association ("School Board")
 PacificCorp
 Center for Energy and Economic Development
 International Brotherhood of Electrical Workers ("IBEW")
 Phelps Dodge
 Department of the Navy on behalf of the Department of the Defense ("Department of Defense")

29 The following parties appeared and presented evidence at the hearing: Citizens; ACAA; IBEW;
 30 TEP; Enron; City of Tucson; Department of Defense; PG&E; Electric Competition Coalition; Goldwater
 31 Institute; Land and Water Fund; Utility Group; Carl Dabelstein; RUCO; AEPCO; Navopache; Arizonans
 32 for Electric Choice and Competition; Arizona Consumers Council; APS; School Board; Attorney
 33 General; Staff; and AUIA. At the conclusion of the hearing, the matter was taken under advisement
 34 pending submission of Opening Briefs on March 16, 1998 and Reply Briefs on March 23, 1998 and the
 35 issuance of a Recommended Opinion and Order to the Commission.

DISCUSSION

Introduction

Pursuant to Decision No. 59943, the Commission approved a phase-in transition to a competitive generation electric power market commencing on January 1, 1999. In the long-run, it is believed that competition will result in lower prices, better service, more choices and increased innovation. However, the transition from regulated monopoly to a competitive market has raised some contentious issues. One of the primary issues is who should pay for the costs associated with the transition from a cost-based regulated environment to a market environment. The Affected Utilities² have claimed a reliance on building large baseline generation plants/long-term power contracts to provide electric service for all those who desired service for a promise of regulated returns over the life of the plant. This is in conflict with market priced rates, especially during a period of excess generation capacity in the Southwest Region. According to APS, there will be excess capacity up through 2006. The difference between market based prices and the regulated cost of power has been generally referred to as "stranded costs". Rates that customers pay today include 100 percent recovery of stranded costs. These stranded costs consist of the following general categories: Generation related assets; Regulatory assets; and Social costs.

Pursuant to the Electric Competition Rules, the Group developed recommendations for the analysis and recovery of stranded costs. The Group held its initial meeting on March 4, 1997. There were several other meetings held during 1997, culminating in a Working Group Report on September 30, 1997. Because of the complexity of the stranded cost issue as well as the diversity of interests, there was little consensus reached by the Group. As a result, an evidentiary hearing was established to address the stranded costs issues.

² Pursuant to R14-2-1601(1), "Affected Utilities" means the following public service corporations providing electric service: Tucson Electric Power Company, Arizona Public Service Company, Citizens Utilities Company, Arizona Electric Power Cooperative, Trico Electric Cooperative, Duncan Valley Electric Cooperative, Graham County Electric Cooperative, Mohave Electric Cooperative, Sulphur Springs Valley Electric Cooperative, Navajo Electric Cooperative, Ajo Improvement Company, and Morenci Water and Electric Company.

Our December 1, 1997 Procedural Order, as amended by our December 11, 1997 Procedural Order, set forth nine issues to be resolved at this time:

1. Should the Electric Competition Rules be modified regarding stranded costs, if so, how?
2. When should "Affected Utilities" be required to make a "stranded cost" filing pursuant to A.A.C. R14-2-1607?
3. What costs should be included as part of "stranded costs" and how should those costs be calculated?
 Sub-Issue No. 3(A): What calculation methodology is recommended, and what assumptions are made including any determination of market price?
 Sub-Issue No. 3(B): Are there any implications of the Statement of Financial Accounting Standards No. 71 resulting from the recommended stranded cost calculation and recovery methodology?
4. Should there be a limitation on the time frame over which "stranded costs" are calculated?
5. Should there be a limitation on the recovery time frame for "stranded costs"?
6. How and who should pay for "stranded costs" and who, if anyone, should be excluded from paying for stranded costs?
7. Should there be a true-up mechanism and, if so, how would it operate?
8. Should there be price caps or a rate freeze imposed as part of the development of a stranded cost recovery program and if so, how should it be calculated?
9. What factors should be considered for "mitigation" of stranded costs?

All of these questions are generally inter-related to the primary issue of how much, if any, of stranded costs should be collected by the Affected Utilities. That issue can be divided into what methodology should be used in calculating stranded costs and how much of those costs should be recovered by the Affected Utilities. Further, we believe Question Nos. 3, 4, 5 and 9 go directly to those issues. As a result, we will initially focus on the following Questions:

- Question No. 3: What costs should be included as part of "stranded costs" and how should those costs be calculated?
- Question No. 4: Should there be a limitation on the time frame over which "stranded costs" are calculated?
- Question No. 5: Should there be a limitation on the recovery time frame for "stranded costs"?

1 Question No. 9. What factors should be considered for "mitigation" of stranded costs?

2 There were a variety of recommendations both as to the method of calculating stranded costs as
3 well as the percentage of stranded costs to be recovered by the Affected Utilities. Generally the
4 methodologies fell into two broad categories: Administrative and Market.

5 The Administrative Category was represented by the Net Lost Revenues approach and the
6 Replacement Cost Valuation approach. The Net Lost Revenues approach compares the future annual
7 generation revenue requirement for the Affected Utility in a competitive market place to the annual
8 requirement under the traditional regulated market. One of the main advantages cited is that it can be
9 periodically trued-up to reflect changes.³ A disadvantage cited was the difficulty of estimating future
10 market prices. The Replacement Cost Valuation approach compares existing generation assets of the
11 Affected Utilities with the most cost-effective technology available today. An advantage is that it
12 estimates the stranded costs over the life of the assets. A disadvantage is that there is no opportunity for
13 a true-up to correct any erroneous assumptions.

14 The Market Category was represented by the Auction and Divestiture approach and the Stock
15 Market approach. The Auction and Divestiture approach would require the Affected Utilities to auction
16 off their generation assets and compare the value received to the net book value of the assets to determine
17 stranded costs. An advantage is that no estimation is required. A disadvantage is the various restrictions
18 that have to be overcome to sell the generation assets. The Stock Market approach requires a new stock
19 class to be formed which would give holders a claim against any stranded costs to be recovered. An
20 advantage is that it does not require any true-up. A disadvantage is that there is no assurance that the
21 stock valuation will have any relationship to stranded costs.

22 While the parties disagreed on the methodology to compute stranded costs, there was even more
23 disagreement as to how much, if any, of the stranded costs should be collected by the Affected Utilities.
24 The computation methodologies were generally tied to a mitigation recommendation. For example, most
25 of the parties advocating the Auction and Divestiture Approach also recommended that Affected Utilities
26 not be allowed stranded cost recovery unless they followed the Auction and Divestiture Approach.

27
28 ³ There were a variety of advantages and disadvantages given for all the categories. For discussion purposes, only one advantage and disadvantage is listed for each of the categories.

1 Some parties recommended the Affected Utilities do all possible mitigation first and then the amount of
2 stranded costs will be determined. There were a variety of proposals that would result in a sharing of
3 stranded costs between customers and shareholders, the rationale being that the best mitigation incentive
4 is for the Affected Utilities to be at risk for a portion of the stranded costs. The Affected Utilities
5 indicated that they have already put forth major mitigation efforts as evidenced by rate reductions over
6 the last several years.

7 Analysis

8 In analyzing the various proposals and the evidence in support of those proposals, we conclude
9 there are several primary objectives which must be taken into consideration in deciding the overall
10 stranded cost issue. Those primary objectives are as follows:

- 11 A. Provide the Affected Utilities a reasonable opportunity to collect 100 percent of their
12 unmitigated stranded costs;
- 13 B. Provide incentives for the Affected Utilities to maximize their mitigation effort;
- 14 C. Accelerate the collection of stranded costs into as short of a transition period as possible
15 consistent with other objectives;
- 16 D. Minimize the stranded cost impact on customers remaining on the standard offer;
- 17 E. Don't confuse customers as to the bottom line; and
- 18 F. Have full generation competition as soon as possible.

19 Our first listed objective is to provide the Affected Utilities a reasonable opportunity to collect
20 100 percent of unmitigated stranded costs. We note that this is consistent with the results in the majority
21 of other states that have decided this issue. Based on past commitments/investments, the Affected
22 Utilities have sunk costs which would be stranded if they exceed market prices. This is not surprising
23 since technology has continued to improve over time resulting in more efficient generation units.
24 Additionally, there are social costs imposed on regulated entities as well as reserve requirements, all of
25 which add to the regulated costs. The Commission has in previous rate cases determined those portions
26 of generation assets which were prudently incurred. In hindsight, some of the managerial decisions may
27 not have been prudent based on subsequent changes in technology. However, we do not find it
28 appropriate to reconsider previous management decisions which the Commission determined were
prudent at the time they were made. While we find the Affected Utilities should have a reasonable

1 opportunity to collect 100 percent of unmitigated stranded costs, we want to emphasize that there is no
2 guarantee just as there is no guaranteed recovery under traditional regulation.

3 It is our second objective to have an incentive that will result in a maximum mitigation effort by
4 the Affected Utilities. Based on the testimony, we believe there should be some type of sharing of
5 stranded costs between ratepayers and shareholders. Further, any sharing percentage would be
6 determined prior to mitigation. Some of the parties had recommended the utilities be required to make
7 every feasible mitigation effort possible and then share the remaining stranded costs. Clearly, that would
8 not provide the Affected Utilities with an opportunity to collect 100 percent of stranded costs but only
9 a pre-established percentage. We believe it is more equitable to establish a method of sharing and then
10 as an incentive the Affected Utilities keep the subsequent mitigation savings.

11 We believe that divestiture of an Affected Utility's generation units would represent a significant
12 mitigation measure, at least based on testimony that recent auctions of generating units in other states
13 have resulted in sales at substantially in excess of book value. For Affected Utilities that do not choose
14 to divest their generation assets, the best incentive to mitigate is for the Commission to create a risk that
15 not all stranded costs will necessarily be recoverable.

16 Our third objective is to minimize the duration of the transition period consistent with other
17 objectives. Generally, most of the parties recommended a transition period somewhere between three
18 to six years. It was also generally recognized that the time period will have to have some flexibility in
19 order to take into account our other listed objectives. A longer transition period will result in a reduced
20 annualized stranded cost amount.

21 The next listed objective is to minimize the stranded cost impact on the customers that remain on
22 the standard offer. One of the main concerns expressed over and over by various consumer groups was
23 that the small consumers would end up with higher costs during the transition phase and all the benefits
24 would flow to the larger users. At the time of the hearing, there had been minimal participation in
25 California by residential customers in the competitive electric market place. It is not the Commission's
26 intent to have small consumers pay higher short-term costs in order to provide lower costs for the larger
27 consumers. Accordingly, we will place limitations on stranded cost recovery that will minimize the
28 impact on the standard offer.

1 We have included the objective regarding confusion because of the results in other states. There
2 appears to have been some confusion whereby customers were told their rates were going down when,
3 in fact, if stranded costs were taken into consideration, the customers total bill actually increased. It is
4 the Commission's intent that customers of the Affected Utilities be given the bottom line results of
5 stranded costs. It should not be called a decrease unless it is a decrease on the overall bill. It also must
6 be understood that a short transition period and rate reductions are in direct contradiction.

7 Lastly, it is the Commission's intent that individual stranded cost proceedings occur as quickly
8 as possible in order to provide an opportunity for full generation competition as soon as possible. Most
9 of the participants recommended the Affected Utilities file their individual stranded cost requests as soon
10 as possible. The proposed time periods ranged from filing before the end of the hearing (City of Tucson)
11 to within 120 days of the date of this Decision (TEP). Because of the January 1, 1999 deadline for
12 commencement of the initial phase for competition, it is imperative that the earliest possible date for
13 filing of individual stranded costs be set. The Affected Utilities have indicated stranded cost filings
14 cannot be made without the additional guidance from this Decision. As a result, we find a reasonable
15 deadline for stranded cost filings by each Affected Utility to be no later than 60 days from the date of this
16 Decision.

17 The conflict between the aforementioned objectives is the reason the stranded cost issue was
18 contentious. At first blush, California appears to have satisfied all these objectives simultaneously.
19 However, what has been declared as a rate reduction disappears when the securitization portion of the
20 California plan is taken into consideration. Securitization does have the effect of reducing the annual
21 transition charge by spreading it over a much longer period of time.

22 As previously noted, we find the Affected Utilities should have a reasonable opportunity to collect
23 100 percent of their stranded costs. Although we cannot go so far as to agree with those parties who
24 advocate that no stranded cost recovery should be allowed for Affected Utilities that do not divest, we
25 do believe that the opportunity for full stranded cost recovery should be available only to those Affected
26 Utilities that choose to divest. For Affected Utilities who do not divest, it is appropriate for the
27 Commission to devise a different approach to deal with a particular set of circumstances. Depending on
28 the situation of given Affected Utility, it may be in the public interest to authorize revenues sufficient to

1 maintain financial integrity, such as avoiding default under currently existing financial instruments during
2 a transition period, or for the Commission to otherwise provide an allocation of stranded costs
3 responsibilities and risks between ratepayers and shareholders.

4 Whatever stranded costs are authorized for recovery for a given Affected Utility, all Affected
5 Utilities are nevertheless expected to make all reasonable efforts to mitigate stranded costs. We
6 recognize there are certain stranded costs which are more difficult to mitigate for which the Affected
7 Utilities should have more of a guarantee than other stranded costs. We find that social costs such as
8 low-income programs, DSM and renewable programs that have been approved by the Commission
9 should be 100 percent recovered. Pursuant to A.A.C. R14-2-1608 those costs are to be collected annually
10 as system benefit charges and as such are not considered stranded costs. Because of the difficulty of
11 mitigating regulatory assets as well as the possible financial implications⁴, we believe they also should
12 be given an assured recovery. These are costs which would have been charged as expenses in a previous
13 period absent an implicit promise by the Commission that they be deferred as an asset and collected from
14 ratepayers in the future.

15 Based on the variety of financial conditions, types and amounts of stranded costs as well as
16 shareholder/customer relationships, we find that no one methodology will fit all Affected Utilities. As
17 a result, we will allow each Affected Utility to choose from two options: Option No. 1 -
18 Divestiture/Auction Methodology; or Option No. 2 - Transition Revenues Methodology. These options
19 are described below:

20 Option No. 1 - Divestiture/Auction Methodology

21 The first option is to determine the amount of stranded costs by
22 divesting/auctioning off all generation assets. In addition to the stranded costs
23 defined by A.A.C. R14-2-1601.8, reasonable costs (i.e., costs incurred only after
24 all reasonable efforts at minimization have been undertaken) incurred for
25 premiums, penalties or other payments necessary to effect divestiture; income tax
26 ramifications of divestiture; redemption costs associated with tax-exempt two-
27 county debt which may have to be redeemed upon transfer of the assets (on-going
increased debt costs will be eligible for recovery through tariffed rates); and other
such reasonable costs necessarily incurred to effectuate divestiture, shall be
recoverable as stranded costs. Unmitigated stranded costs shall also include
reasonable employee severance and retraining costs necessitated by electric

28 ⁴ A decision that results in significant write-offs of regulatory assets could seriously impair
the financial integrity of an Affected Utility.

1 competition, where not otherwise provided.

2 Each Affected utility choosing divestiture must, no later than October 1, 1998, file
3 a divestiture plan for Commission approval. Divestiture must be completed no
4 later than January 1, 2001. Generation assets of Affected Utilities will be sold at
5 divestiture auctions. No Affected Utility may bid on its generation assets being
6 auctioned. However, an Affected Utility's generation affiliate may bid on and
7 acquire the generation assets of its parent or sister company, or the generation
8 assets of another Affected Utility, subject to the following conditions: No entity
9 or its affiliate(s) may purchase generation assets at any divestiture auction unless
10 it is the highest bidder and the acquisition will not result in the entity (including
11 any of its affiliates) having more than 40 percent of state's total generation
12 megawatts of capacity. An Affected Utility that divests all its generation costs to
13 non-affiliated entities, that results in negative stranded costs (not including
14 regulatory assets) as defined by the Commission's Retail Electric Competition
15 Rules and this Order, shall be entitled to keep 50 percent of the negative stranded
16 costs.

17 An Affected Utility shall be permitted to collect 100 percent of its stranded costs,
18 including a return on its unamortized balance, over a ten year period. The
19 Commission will work with the Affected Utility to provide sufficient assurances
20 in order to avoid triggering write-offs. If the stranded cost amount is determined
21 to be negative, ratepayers shall be entitled to receive 100 percent through a refund,
22 negative surcharge, or other mechanism as approved by the Commission. All
23 customers of the Affected Utility shall pay their appropriate share of stranded
24 costs through a CTC, or a standard offer rate. Stranded cost or other transition
25 revenues authorized by the Commission shall be collected over no longer than ten
26 years.

27 Option No. 2 - Transition Revenues Methodology

28 The second option would be to provide sufficient revenues necessary to maintain
financial integrity, such as avoiding default under currently existing financial
instruments for a period of ten years, at the end of which time there would be no
remaining stranded costs, or for the Commission to otherwise provide an
allocation of stranded cost responsibilities and risks between ratepayers and
shareholders as is determined to be in the public interest for a given Affected
Utility.

Individual Stranded Cost Filings

Within sixty days of the date of this Decision, each of the Affected Utilities shall file its choice
of options for stranded cost recovery. In addition, the Affected Utility will need to file an implementation
plan that would include the following items if appropriate for their option choice: the estimation of
stranded costs separated out into regulatory assets and other generational related assets; a preliminary
plan for auction/divestiture; the minimum financial ratios to maintain financial viability for ten years; the
amount of regulatory assets requested, how much of those assets are generation related, and the
Commission Decision No. that approved such assets; and other information as necessary.

Question No. 1: Should the Electric Competition Rules be modified regarding stranded costs, if so, how?

The majority of the parties did not believe the Rules need any significant modifications. However, most parties recommended some minor modification/clarifications.

A.A.C. R14-2-1601(8) ("Rule 1601(8)") contains the following stranded cost definition:

R14-2-1601(8):

8. "Stranded Cost" means the verifiable net difference between:

a. The value of all the prudent jurisdictional assets and obligations necessary to furnish electricity (such as generating plants, purchased power contracts, fuel contracts, and regulatory assets), acquired or entered into prior to the adoption of this Article, under traditional regulation of Affected Utilities; and

b. The market value of those assets and obligations directly attributable to the introduction of competition under this Article.

In general, the Affected Utilities were of the opinion that some post-1996 costs should be fairly included as stranded costs. For that reason, most of the Affected Utilities requested the phrase "acquired or entered into prior to the adoption of the Article" should be deleted. Other parties filed opposition to such a change.

We believe there does need to be a reasonable cutoff period for stranded costs and the approval date of the Electric Competition Rules is a reasonable cutoff. While the Affected Utilities may have additional costs related to transactions in implementing electric competition, those costs, if reasonable, can be factored into the market price. For clarification, the following should be added after "adoption of this Article"; "or after the adoption of this Article if approved by the Commission". In addition, as stated above, the Rule should be clarified that additional costs may also be included in stranded costs, such as costs related to divestiture or to retraining of workers whose jobs are lost because of competition, and costs related to or resulting from divestiture.

A.A.C. R14-2-1607 ("Rule 1607") provides guidance for the recovery of stranded costs. Rule 1607(A) reads as follows:

R14-2-1607(A):

- A. The Affected Utilities shall take every feasible, cost-effective measure to mitigate or offset Stranded Cost by means such as expanding wholesale or retail markets, or offering a wider scope of services for profit, among others.

In general, all the Affected Utilities opposed the requirement to take "every feasible, cost-effective measure to mitigate . . . such as expanding wholesale or retail markets. . . ." According to the Affected Utilities, a more appropriate requirement would be to "make reasonable efforts to mitigate avoidable stranded costs". Further, the Affected Utilities opined that any mitigation should not include revenues from unrelated activities to offset stranded costs.

While it was the Commission's intent for the Affected Utilities to aggressively pursue mitigation efforts, we recognize it is virtually impossible to identify every "feasible cost effective measure". As a result, we agree that Rule 1607 needs to be clarified by replacing "feasible" with "reasonable". As to the request to not include revenues from unrelated activities, we believe no clarification is necessary since the Commission is limited in its jurisdiction.

Rule 1607(B) reads as follows:

R14-2-1607(B): The Commission shall allow recovery of unmitigated Stranded Cost by Affected Utilities.

Several of the non-Affected Utilities requested that Rule 1607(B) be clarified to provide that Affected Utilities will be afforded an opportunity (not a guarantee) to recover legitimate unmitigated stranded costs. There was also a request that Rule 1607(B) be clarified to provide that any stranded cost recovery would commence with the introduction of retail competition.

In reading the Rules as a whole, we believe it is already clear that stranded cost recovery will commence with the introduction of retail competition. We also believe that a reading of the Rules in their entirety places the burden on the Affected Utility to demonstrate they have aggressively pursued mitigation efforts. As a result, the Affected Utility has a high burden of proof regarding its mitigation efforts. If such burden is not met, then the Affected Utility should not be allowed carte blanche recovery. Even the Affected Utilities acknowledged during the hearing that they did not want a guarantee but only a reasonable opportunity for recovery of legitimate unmitigated stranded costs. Accordingly, we will

1 modify Rule 1607(B) by inserting the words "a reasonable opportunity for" after the word "allow".

2 R14-2-1607(G):

3 G. The Affected Utilities shall file estimates of unmitigated Stranded Cost. Such
4 estimates shall be fully supported by analyses and by records of market
5 transactions undertaken by willing buyers and willing sellers.

6 PG&E requested Rule 1607(G) be modified to provide an explicit date for Affected Utilities to
7 file estimates of unmitigatable stranded costs. Electric Choice proposed Rule 1607(G) be modified to
8 provide that stranded cost estimates be filed at least eight months prior to the date of commencement of
9 recovery.

10 As previously discussed, each Affected Utility is being ordered to file its choice of options for
11 stranded cost recovery along with a detailed plan which will include stranded cost estimates.
12 Accordingly, we do find it necessary to change Rule 1607(G).

13 R-14-2-1607(I):

14 A.A.C. R14-2-1607(I) ("Rule 1607(I)") lists various factors to consider in determining the
15 magnitude of stranded costs. AEPCO proposed a prudence exclusion be added to Rule 1607(I).
16 According to AEPCO, such an exclusion will avoid time consuming debate over issues which have
17 previously been settled. AEPCO's proposed language is as follows: "The prudence of an Affected
18 Utilities' investment prior to the effective date of this article which the Commission had a reasonable
19 opportunity to evaluate shall not be at issue in the stranded cost determination."

20 It is not the Commission's intent to go back and revise previous prudency determinations. This
21 does not mean that the Commission may not consider changed circumstances and resulting management
22 decisions subsequent to previous prudency determinations. The Commission does not find it necessary
23 to list a new factor as part of Rule 1607(I) at this time.

24 A.A.C. R14-2-1607(J) ("Rule 1607(J)") provides guidance as to who stranded costs may be
25 recovered from:

26 R14-2-1607(J):

27 J. Stranded Cost may only be recovered from customer purchases made in the
28 competitive market using the provisions of this Article. Any reduction in
electricity purchases from an Affected Utility resulting from self-generation,
demand side management, or other demand reduction attributable to any cause
other than the retail access provisions of this Article shall not be used to calculate

1 or recover any Stranded Cost from a consumer.

2
3 PG&E requested Rule 1607(J) be clarified to indicate that stranded costs are recoverable from all
4 retail generation customers who remain connected to the transmission and distribution systems regardless
5 of the source of power. APS requested a similar clarification and proposed deletion of the first sentence
6 starting with "Stranded Cost may". AEPCO proposed all language after "customer" be deleted.

7 It was the Commission's intent in Rule 1607(J) to make sure customers on the standard offer were
8 not charged stranded costs as part of a transition charge in addition to an identical allocation as part of
9 the standard offer. As a result, all customers connected to the transmission and distribution systems will
10 be paying a share of stranded costs in some form but there will be no double charge allowed. We do not
11 find that any change is necessary to Rule 1607(J).

12 A.A.C. R14-2-1608 ("Rule 1608") provides guidance on what can be collected as a system benefit
13 charge.

14 R14-2-1608:

- 15 A. By the date indicated in R14-2-1602, each Affected Utility shall file for
16 Commission review non-bypassable rates or related mechanisms to recover the
17 applicable pro-rata costs of System Benefits from all consumers located in the
18 Affected Utility's service area who participate in the competitive market. In
19 addition, the Affected Utility may file for a change in the System Benefits charge
20 at any time. The amount collected annually through the System Benefits charge
21 shall be sufficient to fund the Affected Utilities' present Commission-approved
22 low income, demand side management, environmental, renewables, and nuclear
23 power plant decommissioning programs.

24 According to APS, nuclear fuel disposal costs are an inherent part of nuclear decommissioning
25 costs which are recoverable through the System Benefits charge. As a result, APS requested Rule
26 1608(A) be clarified to specifically include the recovery of nuclear disposal costs. ACAA and RUCO
27 proposed that nuclear fuel disposal and decommissioning charges are directly related to generation and
28 as a result should be part of stranded costs not system benefits.

25 We concur with APS that nuclear fuel disposal costs are an inherent part of nuclear
26 decommissioning costs. Further, for public health and public safety reasons we do not believe these
27 should be lumped in with stranded costs. We believe Rule 1608(A) is clear without the change proposed
28 by APS.

1 Question No. 3: What are the Implications of FAS 71?

2 The Affected Utilities must prepare their public financial statements in accordance with Statement
3 of Financial Accounting Standard No. 71, Accounting for the Effects of Certain Types of Regulation
4 ("FAS 71"). Pursuant to FAS 71, the Commission can create an asset by deferring, for future recovery,
5 a current cost that would otherwise be charged to expense. These are referred to as regulatory assets and
6 may continue to be reflected on a utility's books and financial statements as long as the following criteria
7 are met: 1) It is probable that future revenue in an amount at least equal to the capitalized cost will result
8 from inclusion of that cost in rates; and 2) Based on available evidence, future revenue will be provided
9 to permit recovery of the previously incurred cost rather than to provide for expected levels of similar
10 future costs.

11 According to the Affected Utilities, the financial community is looking for assurances from the
12 Commission that the Affected Utilities will be provided a return on and return of their investments.
13 Without such assurances, the Affected Utilities will have to write-down and/or write-off some of the
14 investments.

15 Most of the parties acknowledged that regulatory assets need to be treated differently than
16 generation assets. However, some of the non-Affected Utilities opined that accounting rules should not
17 drive regulatory policy. We believe the stranded cost recovery mechanisms approved herein will provide
18 the Affected Utilities sufficient revenues to enable them to recover the appropriate regulatory assets.
19 Accordingly, there should be no necessity for write-downs and/or write-offs.
20

21 Question No. 7: Should there be a True-up Mechanism and, if so, How Would it Operate?

22 Most of the parties tied the need of any true-up to the stranded costs methodology they
23 recommended. There were concerns expressed that a true-up mechanism could result in
24 uncertainty/confusion for customers and thus inhibit competition. In general, the non-Affected Utilities
25 believed a downward true-up mechanism was a good idea.

26 Of the options approved herein, Option 1 requires a true-up. In addition, Option 2 may require
27 a true-up to the extent that the Commission authorizes recovery of a particular amount of stranded costs.
28 The requirements of any true up mechanism should be established at the time the Commission acts on

1 an Affected Utility's stranded cost filing.

2 Question No. 8: Should there be a Price Cap or Rate Freeze?

3 Generally, the Affected Utilities opposed any price cap or freeze. On the other hand, many of the
4 other parties supported a price cap but not a rate freeze. Those parties representing various small
5 consumers were especially vociferous about having some type of price cap. There was a concern that
6 larger users would reap all the benefits of competition while the smaller users would bear the brunt of
7 higher costs.

8 We share the concerns expressed by small consumer groups. If small consumers are not going
9 to have benefits in the short run, they should not be unfairly burdened with increased rates resulting from
10 the transition costs. While we agree that small consumers deserve some rate protection during the
11 transition period, we are also concerned that the transition costs may require some increase. We have
12 placed a limitation that customers on the standard offer will not receive an increase as a result of stranded
13 costs. Any stranded costs which would result in an increase to the standard offer will have to be deferred
14 to a future period. However, an Affected Utility can still file a rate case and request an increase for
15 reasons other than stranded costs during the transition period.

16 We also share concerns that stranded costs should not be used to discourage the marketing of
17 competitive generation. We have placed a limitation that no customer will receive a rate increase as a
18 result of stranded costs.

19 Miscellaneous

20 A. School Board Variance/Exemption:

21 The School Board requested a variance/exemption for its share of any stranded costs. According
22 to the School Board, its request should be granted because of the school funding crisis in Arizona and
23 because it is in the public interest. Further, the School Board asserted that its proposal would not result
24 in any cost-shifting between or within customer classifications as the economic burden would be borne
25 by the Affected Utility or its shareholders.

26 Other parties opposed the School Board's request because it would result in preferential treatment
27 which would be unlawful and if granted, the request would open the floodgates for every worthwhile
28 enterprise to claim a similar exemption.

1 We do not agree with the School Board's assertion that their proposal would not result in cost
2 shifting. Clearly, either other ratepayers and/or other shareholders would pick up the additional costs.
3 Any solution to the School Board funding problems must be dealt with by the legislature on a state-wide
4 basis. Accordingly, the requested variance/exemption is denied.

5 B. Allocation Methodology:

6 There were some discussions regarding the allocation methodology for stranded costs. It is the
7 Commission's intent that all present and future customers should pay their fair share of stranded costs.
8 As a result, we will adopt a rebuttable presumption that all customers connected to the grid should pay
9 an appropriate amount of stranded costs consistent with the current approved rate treatment of each
10 Affected Utility.

11 C. Exit Fees:

12 Several of the parties expressed an interest in an exit fee that would enable them to make an up-
13 front buy out of their portion of stranded costs. We will order each Affected Utility to develop a
14 discounted stranded costs exit methodology that a customer may choose to determine an amount in lieu
15 of making monthly payments. The methodology should be developed with input from interested parties
16 and approved by the Commission.

17 SUMMARY

18 Pursuant to Decision No. 59943, the Commission committed to electric generation competition
19 commencing on January 1, 1999. There are still details which must be resolved prior to such
20 competition. The most contentious issue still needing to be resolved is that of stranded costs. In general,
21 the Affected Utilities have indicated they have the right to such costs because they have followed the
22 "rules of the game." Most of the larger consumers are saying the rules of the game have changed and
23 the remaining baggage from the previous game is the problem of the Affected Utility. The smaller
24 consumers aren't as concerned with the rule changes but do not want to be declared the losers before the
25 game begins.

26 The Commission has attempted in this Decision to carefully balance the various concerns. As
27 a result, we believe the Affected Utilities will have a reasonable opportunity to collect 100 percent of
28 their stranded costs over a relatively short transition period, customers who desire to utilize a competitive

1 generation source will have an opportunity to obtain a more favorable rate than can be obtained through
 2 the standard offer, and those customers who remain on the standard offer will not receive a rate increase
 3 as a result of stranded costs. We want to make it clear that this overall scenario is only possible through
 4 continued growth in Arizona as well as increased efficiencies by the Affected Utility. Growth will help
 5 Affected Utilities mitigate potential losses of customers to competition. At the same time, the Affected
 6 Utilities will need to continue to tighten their belts in order to bring their costs down to the market by the
 7 end of the transition period. After the Affected Utilities have collected the expenses associated with their
 8 appropriate regulatory assets, all customers remaining on the standard offer should receive a reduction
 9 in their overall rates.

10 * * * * *

11 Having considered the entire record herein and being fully advised in the premises, the
 12 Commission finds, concludes, and orders that:

13 FINDINGS OF FACT

- 14 1. The Commission issued Decision No. 59943 which approved the Electric Competition
 15 Rules.
- 16 2. Decision No. 59943 approved a phase-in transition to a competitive generation power
 17 market commencing on January 1, 1999.
- 18 3. In the long-run it is believed that competition will result in lower prices, better service,
 19 more choices, and increased innovation.
- 20 4. The Commission issued Decision No. 60351 which directed the Hearing Division "to
 21 produce procedural orders in order to establish hearings, evidentiary or otherwise, regarding any aspect
 22 of electric competition that is necessary and appropriate".
- 23 5. On September 30, 1997, the Group filed its Report to the Commission.
- 24 6. On October 30, 1997, RUCO filed a Request for Hearing.
- 25 7. Our December 1, 1997 Procedural Order set an evidentiary hearing on generic issues
 26 related to stranded costs commencing on February 9, 1998.
- 27 8. The difference between market based prices and the cost of regulated power has been
 28 generally referred to as stranded costs.

9. According to APS, there will be excess generation capacity in the Southwest Region up through 2006.

10. Stranded costs consist of the following general categories: Generation related assets; Regulatory Assets; and Social costs.

11. The September 30, 1997 Working Group Report contained little consensus on stranded cost issues.

12. Our December 1, 1997 Procedural Order, as amended by our December 11, 1997 Procedural Order, set forth nine issues to be resolved:

Question No. 1. Should the Electric Competition Rules be modified regarding stranded costs, if so, how?

Question No. 2. When should "Affected Utilities" be required to make a "stranded cost" filing pursuant to A.A.C. R14-2-1607?

Question No. 3. What costs should be included as part of "stranded costs" and how should those costs be calculated?

Question No. 3A. What calculation methodology is recommended, and what assumptions are made including any determination of market price?

Question No. 3B. Are there any implications of the Statement of Financial Accounting Standards No. 71 resulting from the recommended stranded cost calculation and recovery methodology?

Question No. 4. Should there be a limitation on the time frame over which "stranded costs" are calculated?

Question No. 5. Should there be a limitation on the recovery time frame for "stranded costs"?

Question No. 6. How and who should pay for "stranded costs" and who, if anyone, should be excluded from paying for stranded costs?

Question No. 7. Should there be a true-up mechanism and, if so, how would it operate?

Question No. 8. Should there be price caps or a rate freeze imposed as part of the development of a stranded cost recovery program and if so, how should it be calculated?

Question No. 9. What factors should be considered for "mitigation" of stranded costs?

13. The methods of calculating stranded costs falls into two broad categories: Administrative and Market.

14. The Administrative Category was represented by the Net Lost Revenues approach and the

1 Replacement Cost Valuation approach.

2 15. The Market Category was represented by the Auction and Divestiture approach and the
3 Stock Market approach.

4 16. Each of the categories and respective approaches have some advantages and
5 disadvantages.

6 17. Rate reductions over the last several years reflect mitigation efforts put forth by the
7 Affected Utilities in contemplation of competition.

8 18. Affected Utilities should have a reasonable opportunity to collect 100 percent of their
9 unmitigated stranded costs.

10 19. Both regulatory assets and the costs of systems benefits should be recovered at 100
11 percent.

12 20. Traditional regulation does not guarantee 100 percent recovery of costs but only a
13 reasonable opportunity to recover costs.

14 21. A longer transition period will result in a reduced annualized stranded cost amount.

15 22. Securitization is a financing method that can be utilized to spread stranded costs over a
16 longer period and thus minimize the annual impact.

17 23. A short transition period and rate reductions are in direct contradiction.

18 24. Regulatory assets are costs which would have been charged as expenses in a previous
19 period absent an implicit promise by the Commission that they be deferred as an asset and collected from
20 ratepayers in the future.

21 25. No one methodology for calculating stranded costs will fit all Affected Utilities.

22 26. Any stranded cost recovery methodology must balance the interests of the Affected
23 Utilities, ratepayers, and a move toward competition.

24 27. The Net Revenues Lost Methodology proposed by APS provides little incentive for
25 customers to utilize another competitive service.

26 28. Affected Utilities should be given more of an assured recovery for regulatory assets and
27 social costs than for other generation related stranded costs.

28 29. All current and future customers of the Affected Utilities should pay their fair share of

regulatory assets and social costs.

30. Arizona's population has been steadily growing.

31. Customer growth will help Affected Utilities mitigate stranded costs.

32. The stranded cost options approved herein should provide sufficient cash flow for the Affected Utilities to recover their appropriate-regulatory assets.

33. Stranded cost recovery is not an opportunity to revisit prudence of previous generation asset decisions.

34. Stranded cost or other transition revenues authorized by the Commission should be collected over no longer than ten years, although particular circumstances and objectives may dictate a shorter or longer period.

35. A reasonable deadline for stranded cost filing by each Affected Utility is no later than 60 days from the date of this Decision.

CONCLUSIONS OF LAW

1. The Affected Utilities are public service corporations with the meaning of the Arizona Constitution, Article XV, under A.R.S. §§ 40-202, -203, -250, -321, -322, -331, -332, -336, -361, -365, -367, and under the Arizona Revised Statutes, Title 40, generally.

2. The Commission has jurisdiction over the Affected Utilities and of the subject matter contained herein.

3. Notice of the proceeding has been given in the manner prescribed by law.

4. The Electric Competition Rules should be amended consistent with this Decision.

ORDER

IT IS THEREFORE ORDERED that within 60 days of the date of this Decision, each Affected Utility as defined in A.A.C. R14-2-1601(1) shall file its choice of options for stranded cost recovery.

IT IS FURTHER ORDERED that each Affected Utility shall file an implementation plan with its stranded cost option which should set forth the details for its plan including its estimated stranded costs separated out into regulatory assets and other generation related assets.

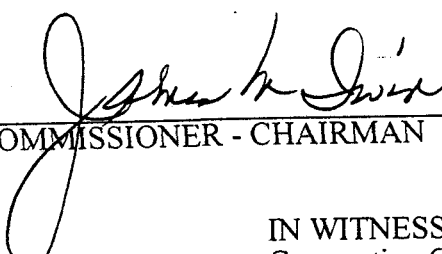
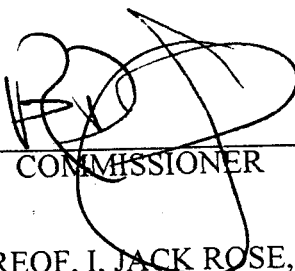
IT IS FURTHER ORDERED that within 30 days of each Affected Utility filing its implementation plan, all other parties shall file any comments/disagreements and requests for hearing.

1 IT IS FURTHER ORDERED that there is a rebuttable presumption that stranded costs shall be
2 allocated in a manner consistent with the current rate treatment for each Affected Utility.

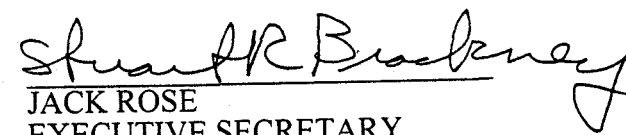
3 IT IS FURTHER ORDERED that the Director of the Utilities Division shall submit rule
4 amendments as set forth herein to the Secretary of State's office commencing the process of rule adoption
5 on an emergency basis.

6 IT IS FURTHER ORDERED that this Decision shall become effective immediately.

7 BY ORDER OF THE ARIZONA CORPORATION COMMISSION.

8
9
10  
11 COMMISSIONER - CHAIRMAN COMMISSIONER COMMISSIONER

12 IN WITNESS WHEREOF, I, JACK ROSE, Executive Secretary of the Arizona
13 Corporation Commission, have hereunto set my hand and caused the official seal
14 of the Commission to be affixed at the Capitol, in the City of Phoenix, this
15 22 day of June, 1998.

16 for 
17 JACK ROSE
18 EXECUTIVE SECRETARY

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DISSENT 
JLR:dap

SEE ATTACHED CONCURRING OPINION OF COMMISSIONER RENZ D. JENNINGS

SERVICE LIST FOR:

DOCKET NO.:

COMPETITION IN THE PROVISION OF
ELECTRIC SERVICES THROUGHOUT THE
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RE-00000C-94-165

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CONCURRING OPINION

NAME: Competition in the Provision of Electric Services throughout the State of Arizona

DOCKET NO. RE-00000C-94-165 OPEN MEETING DATE: June 3, 1998

PREPARED BY: Commissioner Renz D. Jennings



=====

I agree with much of what Commissioner Kunasek writes in his dissenting opinion. However, I don't believe that "all generation in the state would be up for auction at the same time." Even if all affected utilities divest, there probably will be different timing for each divestiture. Moreover, there is little generation up for sale at this moment in the West and the evidence was that many might be willing to pay a premium to get a foothold in new markets. However, I disagree with his assertion that the majority decision constitutes a coerced divestiture. It simply encourages Arizona's utilities to divest by permitting them to keep 50% of the above-book proceeds should they decide to divest. Commissioner Kunasek's assertion that the Order "removes from the bid process the party most likely to bid the highest for its facilities" is flat wrong. Under my amendment to the Order, which Commissioner Kunasek voted against, generation affiliates of incumbent utilities are given the opportunity to bid on the assets of their parent or sister company.

The second purpose of my amendment is the realization that it is important in a competitive generation market to have structural separation of generation to prevent cross-subsidization. My amendment also addresses the market power problem by limiting the ownership of generation serving the Arizona market to 40% by any entity or its affiliates.

DISSENT OPINION

COMPANY: In The Matter Of The Competition In The Provision Of Electric Services
Throughout The State of Arizona

DOCKET NO. RE-00000C-94-0165 OPEN MEETING DATE: 6-3-98

PREPARED BY: Commissioner Carl J. Kunasek



Four years ago I ran for this office promising to deregulate Arizona's electricity market. My commitment to a deregulated market place for energy has grown stronger; however, my appreciation for the complexities of the task and its potential impact on our citizens has deepened. And while many have put this state's deregulation effort on fast forward with promises of rate reductions that may never materialize, I remain committed to an orderly process that will bring about an appropriate market structure and the chance for all Arizona citizens to benefit both early on and when the market is fully competitive.

No one should doubt my commitment to a competitive electricity market. As a legislator, I led the charge to deregulate hospitals, authored the Arizona Health Care Cost Containment System (AHCCS) program, Arizona's answer to Medicaid, and rewrote the laws pertaining to the care and treatment of mentally retarded citizens which removed the provision of state treatment to the private sector. In each of these cases every citizen of the state benefited by switching from government controlled services to services provided by the private sector on a competitive bid basis.

My commitment to deregulating Arizona's power generation market and belief that it will benefit all Arizona citizens, if done right, is no less real. My guiding principle is that all Arizona citizens must have the opportunity to benefit from this change in market structure. We must preserve the finer aspects of the regulated market (reliability and certainty of delivery) and institute a set of rules that provides choice for all Arizonans on a reasonable time line and in an orderly fashion.

For the past two years this Commission has attempted to advance the cause of deregulation by holding numerous workshops as well as hearings on stranded investment that provided all parties the opportunity to meaningfully participate in the decision making process. Much was accomplished along the way but even more needs to be done.

I continue to believe that the best hope for competition and the most beneficial result for Arizona's citizens rest with a settlement that would recognize the needs, strengths and limitations of all classes of customers. For the past 87 years consumers

have had their energy decisions made for them. It is simply unrealistic to expect residential consumers to make informed beneficial decisions overnight. I do concur with staff's position that those not eligible for open access should receive some financial benefit during the time period they are held captive.

I concur with Commissioner Jennings comments (Minutes of Meeting ("MM") page 28 lines 3-12 and lines 16-24) that residential consumers are not clamoring for competition. I also believe that there will come a day when residential consumers will value choices. But that day is not today nor is it in the near future. The market must be given time to evolve and consumers must be given time to learn. What we must not do is take actions that force competition quickly, perhaps haphazardly, that results in the first taste of competition being a sour one for small consumers.

There are many issues yet to be decided. Without question the most controversial issue is stranded investment, the significance of which changes depending on the manner and timing of the transition to competition. I do not believe that these issues can be decided in a vacuum, nor do I believe that the parties can make an informed decision without knowing what comes next. I think it's very important for this Commission and all the parties to weigh the pros and cons of any proposal in context of how it fits in the overall plan. As Michael Grant indicated in his comments (MM, page 100, line 25 through page 101, line 6) we should not be taking issues off the table at this time.

Further, given the significance of the stranded investment outcome, this Commission acts irresponsibly when it approves coerced divestiture on a one-size-fits-all approach without so much as one piece of evidence or analysis in the record that supports the general theme proffered by the majority that divestiture will reduce the amount of stranded investment that residential consumers will pay. Worse yet, divestiture could well increase the amount of stranded investment if utilities are forced to sell facilities in a market saturated with available generation.

Common sense would tell you that if all utilities avail themselves of the divestiture option that all generation in the state would be up for auction at the same time. This is similar to a homeowner trying to sell his home at the very time each of his neighbors had their home on the market. The timing of the sale would not be conducive to producing a high price at the time of sale. Additionally, the order removes from the bid process the party most likely to bid the highest for its facilities. There is simply no reason to deny incumbent utilities the opportunity to retain their assets. ~ -

Let me make it clear that I believe divestiture can be an appropriate method for dispensing with the stranded investment issue. Divestiture must not be coerced or forced. Further, we must recognize that it may not be beneficial for some utilities to divest its generation. As Commissioner Jennings indicated (MM, page 28, line 16-24), without an understanding on where this process ends, the decision to divest "may be less than optimal."

In the final analysis, the action that this Commission took in approving the stranded investment order significantly narrows our options. Further, in our haste to accelerate competition, we run the risk of slowing the transition given certain litigation. I don't think there is anyone familiar with this process that believes that the action taken by this Commission would withstand a legal challenge. This Commission is far better served to carefully evaluate and move forward proposals that will withstand judicial scrutiny so that in the end we don't inadvertently slow the process.